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STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

CHIEF CLERK'S OFFICE

Illinois Bell Telephone Company)	
)	
Application for Review of Alternative Regulation Plan)	Docket No. 98-0252
)	
Illinois Bell Telephone Company)	
)	
Petition to Rebalance Illinois Bell Telephone Company's Carrier Access and Network Access Line Rates)	Docket No. 98-0335
)	
Citizens Utility Board, People of the State of Illinois)	Docket No. 00-0764
v.)	
Illinois Bell Telephone Company)	(Consol.)

**Z-TEL COMMUNICATIONS OPPOSITION
TO THE JOINT MOTION TO REOPEN THE RECORD**

Z-Tel Communications, Inc. ("Z-Tel") strongly, yet respectfully, opposes the Joint Motion of the Illinois Bell Telephone Company ("SBC/Ameritech") and the Citizens Utility Board, the People of the State of Illinois, the City of Chicago, the City of Chicago, and the Cook County State's Attorney's Office (hereinafter collectively referred to "GCI/City Petitioners") to Reopen the Record in the above-referenced dockets. The proposed Plan that Ameritech and the GCI-City petitioners present is riddled with anticompetitive consequences, and improperly and prematurely terminates Condition 26 from the Ameritech/SBC Merger Order. The Commission should deny the Joint Motion.

When the Illinois Commerce Commission approved the merger of SBC and Ameritech, it decided in Condition 26 that the cost savings of the merger would be passed on to Illinois consumers. The Joint Petition seeks to eliminate that Merger Condition in exchange for a one-

time payment that is potentially insufficient to capture the complete merger savings and is certainly discriminatory against CLECs.

Hidden within this one-time, "feel-good" refund plan could lie an SBC/Ameritech Trojan Horse. In particular, SBC/Ameritech may utilize this potential settlement as a substantial marketing tool so as to entrench its position in the market, by luring customers back to Ameritech in exchange for the value of a dinner and a movie for two. In doing so, the plan could do substantial damage to the competitive environment in Illinois – just when competition for mass-market residential and small business consumers has begun.

In these comments, Z-Tel focuses upon two issues – the legal problem associated with the proposal to eliminate Condition 26, and the discrimination problems evident from the Joint Petition proposal.

I. ABOUT Z-TEL AND Z-TEL'S INTEREST

Z-Tel is one of the nation's largest competitive local exchange carriers, with over 250,000 *residential* lines in service in over 30 states nationwide. Z-Tel's flagship product, Z-LineHOME, is an innovative bundle of local, long distance, and enhanced services to residential consumers. Z-Tel has been actively marketing in Illinois for several months, utilizing an integrated mass-market advertising campaign that includes billboards along interstate highways, radio, and television advertisements.

Illinois is one of Z-Tel's fastest-growing markets. Illinois is the *first* state in which Z-Tel launched its Z-LineBUSINESS service, in part because of the pro-competitive telecommunications environment instilled by the Commission and the recent rewrite of the Illinois Public Utility Act. Z-Tel is spending a disproportionate share of its marketing dollars in Illinois because it believes in the growth potential in Illinois for its innovative and cost-effective services.

Competitive entry in the mass market in Illinois is at nascent and precarious levels. Z-Tel is focused on serving residential and small business consumers and has chosen to make Illinois one of its key target markets in the coming year because of the competitive opportunities offered by the Commission, the Merger Conditions, and the recent telecom law re-write. Z-Tel's initial market success is, however, threatened if SBC/Ameritech is allowed to stack the deck.

In particular, mass-market entry would be harmed if the Commission eliminated Condition 26 by putting in place a rebate plan that would build in competitive advantages to SBC/Ameritech. As discussed in Section III below, Z-Tel believes that the proposal set forth by Joint Petitioners is in fact highly discriminatory and would cause significant disruption to the nascent competition that is developing in Illinois to this mass market.

With mass-market entry at its early stages, there is significant potential for SBC/Ameritech to nip these emerging choices at the bud. An enticing and Commission-blessed "one-time credit" for "switching back" to SBC/Ameritech could substantially undermine the current efforts of entrants to build share in Illinois in the mass market.

As a result, Z-Tel opposes the motion to reopen the record in this proceeding. Upsetting the competitive balance in the state poses far greater risk to consumers than promised by the Joint Petition.

II. THE PROPOSAL TO TERMINATE CONDITION 26 IS INCONSISTENT WITH SECTION 7-204(C) OF THE ILLINOIS PUBLIC UTILITIES ACT.

It is important to understand how the Commission reached this point. In August 1998, in their initial Application for Merger, SBC and Ameritech vehemently denied that Illinois law

required that the cost savings of the transaction be allocated to consumers.¹ SBC and Ameritech stuck to that position throughout the merger proceeding, even during the mandated rehearing in the summer of 1999.

The Commission soundly rejected that view, stating that a plain reading “inevitably leads us to the conclusion that it applies in this case.” Merger Order at 143. The Commission went on to note that rewriting the statute “is within the exclusive province of the General Assembly, and not the Commission.” *Id.* at 143-44. While the Commission noted that it had discretion in how to allocate the merger savings but that its allocation decision “must be guided by sound legal judgment.” Merger Order at 145.

In the end, the Commission recognized the adverse impact to competitors that would result from the merger and specifically ordered that 50% of the merger-related savings would inure to carriers that purchased UNEs, interconnection and transport and termination services on a wholesale basis from SBC/Ameritech as well as SBC/Ameritech retail customers. Merger Order at 146-47, Condition 26. The Commission also required that a neutral, third-party auditor would be charged with determining the cost savings from the merger until an updated price cap formula was developed in this Docket 98-0252.

The Joint Petition seeks to upset that process by replacing Condition 26 in its entirety. The Joint Petition does not set out a plan for a permanent cost savings mechanism in this Docket 98-0252 and instead asks the Commission to wash its hands of the entire matter in exchange for a one-time payment.

¹ See Direct Testimony of David H. Gephardt, ICC Docket No. 98-0555 at 20 (“the appropriate result would be *no allocation* of savings. . . . Section 204(b) does not include any legislative invitation to require public interest “benefits” or otherwise interfere with the marketplace forces which drive mergers of this kind.”).

Even without considering the clear inadequacy of the one-time payment, it is not clear that the Commission can accept this deal and still comply with Section 7-204(c). As the Commission determined in the Merger Order, it was required to by Section 7-204(c) to consider cost savings from the transaction and ensure that those savings be passed through to SBC/Ameritech's customers. As discussed above, the Commission noted that it did not have discretion to rewrite the statute. To ensure that the statute was complied with, the Commission implemented Condition 26, which set forth a rational method of determining and ensuring that the cost savings be passed on to SBC/Ameritech customers in Illinois. The third-party audits were a crucial component of Condition 26 and those audits provided a useful check against some fairly aggressive accounting techniques of SBC/Ameritech in this regard.

Joint Petitioners do not provide any reason to believe that Section 7-204(c) would be satisfied by their proposed one-time payment. Joint Petitioners provide no basis to support the \$197 million figure – only a vague assurance that it will provide such evidence if the proceeding is re-opened. But what if, in two years, the cost savings from the transaction were actually significantly greater? In fact, since the Joint Petition would eliminate tracking and reporting procedures, there would be *no way* for the Commission to be sure that the merger savings are not, in fact, much greater than this amount. If the Commission does as Joint Petitioners ask, the Commission would cede its only tool to ensure that Section 204(c) has been satisfied. It is difficult to imagine how the Commission could justify this action as complying with its statutory mandate.

III. THE JOINT PETITION PLAN PRESENTS SIGNIFICANT ANTICOMPETITIVE OPPORTUNITIES FOR SBC/AMERITECH

SBC/Ameritech and the GCI/State petitioners proposal for a one-time \$197 million “credit by Ameritech Illinois to its customers” is unspecific and could potentially do more harm than good. In fact, because the plan seems to systemically discriminate against wholesale providers, the plan could be a Trojan Horse that could adversely impact competition in Illinois. In the end, Illinois consumers could be significantly worse off than without the plan – because the damage to competition may significantly outweigh the one-time benefits of the credit.

The Proposed One-Time Credit Discriminates Against CLECs. The Joint Petition notes that the one-time credit “will be issued to eligible end users, interexchange carriers and CLECs purchasing UNEs, interconnection, transport and termination service based on the relative revenues Ameritech Illinois received from these customer groups in calendar year 2001.” The Joint Petition defines “eligible end users” to “include residence customers and small business customers with 4 lines or less.”

As proposed by Joint Petitioners, the rebate mechanism **by definition** discriminates in favor of SBC/Ameritech’s retail services by according, on a per-line basis, retail customers a larger share of the cost savings than wholesale customers. This is because “wholesale revenues” per line are always lower than “retail revenues” per line. As a result, apportioning by means of “revenues” by definition means that the credit apportioned to wholesale customers will **always** be lower on a per-line basis than retail customers.

Consider, for example, that the retail revenue to SBC/Ameritech for a local residential dialtone line is \$30/month, while the wholesale revenue SBC/Ameritech could generate for that same line through a UNE-P arrangement is \$20/month. As proposed by Joint Petitioners, the one-time rebate available to the SBC/Ameritech retail customer would be **fifty percent higher** than the one-time rebate allocated to the wholesale UNE-P service provider. The UNE-P CLEC would simply not be able to match SBC/Ameritech’s Commission-blessed, one-time

rebate without dipping into its own cash. SBC/Ameritech should be expected to exploit this inherent "rebate advantage" to the hilt.

In other words, the Commission would put in place a "merger savings" credit regime that would **encourage consumers to return to SBC/Ameritech**. This is not competition – it is SBC/Ameritech utilizing a Trojan Horse regulatory mechanism to entrench further its dominant market position.

In addition, the rebate structure discriminates against CLECs like Z-Tel that focus their market entry efforts on residential and small business consumers. As proposed by Joint Petitioners, the CLEC share of the rebate would be calculated by reference to the entire wholesale revenue to SBC/Ameritech from *all* CLEC operations services – even those CLEC operations and services that do not focus on residential and small business consumers.

Indeed, the cost of building out a collocation space may be treated by the plan as "revenue" from "interconnection", but its connection to providing service to residential and small business customers may be nonexistent if that collocation space is not utilized by the new entrant to serve eligible end-users. For example, the wholesale revenue collected by SBC/Ameritech for 1,000 residential UNE-P lines from a CLEC at a cost of \$20/month per line would receive the same portion of the refund as a CLEC that paid SBC/Ameritech \$20,000 to build-out a collocation site with the intention of serving large businesses with fiber. In fact, the same refund would apply to both CLECs -- even if that collocation site were not used to provide service to any end-user in calendar year 2001.

The costs of these large-scale wholesale projects like collocation or entrance facilities would easily swamp residential service provided by a CLEC like Z-Tel, even though Z-Tel has thousands of residential lines in Illinois. As a result, the Joint Petitioner's plan dilutes the impact the one-time credit would have for service providers that focus on residential and small business

customers. This situation would further exacerbate the problem noted above in which the refund granted to CLECs that serve eligible end-users would in no way be able to match the refund SBC/Ameritech would be able to offer its eligible end-users.

A Discriminatory Credit Plan Would Threaten Competition. As discussed above, for several reasons, the credits available to CLECs under the plan would not – under *any* scenario – be as large as the credits that SBC/Ameritech would be granting its own eligible end-users.

Z-Tel is strongly concerned that this one-time credit will simply give SBC/Ameritech the opportunity to rev up its well-oiled “Winback” marketing machine. SBC has an aggressive program that appears to utilize customer disconnect information to lure customers that have left for a CLEC to return to SBC. A Commission-approved “one-time credit” would provide SBC a competitive leg up in this Winback efforts – a credit that competitors could not, by definition, match with their own merger-savings rebate.

The Commission must understand that mass-market competition in Illinois is only beginning to emerge and that CLECs – suffering from a hostile capital environment – are being bled dry by incumbents like SBC/Ameritech. SBC/Ameritech is already advertising heavily in greater Chicagoland that switching to a CLEC is a “Bad Idea.” As a result, SBC is leveraging its own acknowledged faults in providing poor OSS to CLECs as a marketing tool to keep its dominant market share. Adding a \$50 “ICC-mandated rebate” to the mix – a rebate that CLECs would in no circumstances be able to match – would tip the scales even further in the direction of SBC/Ameritech. Because mass-market competition in Illinois is only beginning to develop, there is significant adverse potential impact on competition by incenting consumers to switch back or remain at SBC/Ameritech at this point in time. In the end, the Joint Petition’s plan could hand a marketing advantage to SBC/Ameritech under the guise of a public-spirited

“rebate” — but in the long run, consumers could be substantially worse off if this rebate scheme thwarts competitive entry at this crucial, developmental moment.

Suggestions for Improvement. As noted in Section II above, Z-Tel does not believe that it is procedurally proper for the Commission to reopen this proceeding at this time. Z-Tel believes that the current process of annual audits of merger savings is appropriate, at least for the next several years until the full scale and extent of the merger savings are understood and accounted for. Section 7-204(c) calls for no less.

Nevertheless, if such action is taken, Z-Tel will be an active participant in this process. In doing so, Z-Tel will advance at least two suggestions that would improve operation of the one-time credit.

First, the credit should be allocated **not** on the basis of revenues but on analog dialtone lines and loops provided to CLECs and eligible end users by SBC/Ameritech. Applying a credit in this manner is superior to allocating on a revenue basis because it would apportion the **same** per-line share of the credit to CLECs as SBC/Ameritech retail customers. The discriminatory impact of the revenue allocation proposal (which provides a smaller per-line refund to a wholesale customer as a retail customer) would largely be avoided if the credits were calculated in this fashion.

Second, SBC/Ameritech should be prohibited from utilizing the one-time credit in its retail marketing. Advertisements, customer letters, telemarketing scripts, and bill inserts need to be screened and reviewed to ensure that SBC/Ameritech does not utilize the pending nature of the refund to entice customers to either stay with SBC/Ameritech or to come back to the ILEC. Given the recent publicity about the Joint Petition proposal, the Commission should act swiftly in this matter and begin to take action while this action is pending. Z-Tel suggests that a Declaratory Ruling by the Commission in this proceeding that any such mention or use of the

refund to "winback" customers would be a violation of 13-801 as an act intended to impede competition.

IV. CONCLUSION

Z-Tel has several significant competitive concerns with reopening this proceeding and the Joint Proposal. In particular, as set forth in the Joint Motion, the proposal would cut short the process established by Condition 26 without adequate examination as to whether the one-time payment process adequately fulfills the statutory mandate of Section 7-204(c).

More importantly, the Joint Proposal is discriminatory on its face and could have significant adverse impact on mass-market competition in Illinois. As discussed above, the rebate accorded to CLEC wholesale customers will be, by definition, *lower* than the rebate provided to SBC/Ameritech retail customers for the same line or service. CLECs would have no ability to match this rebate. Given its aggressive anti-CLEC marketing campaign, SBC/Ameritech should be expected to exploit this "rebate debate" to its commercial advantage by touting and publicizing this rebates in its Winback campaigns.

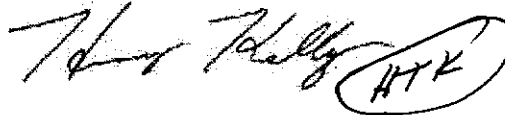
Mass-market competition for residential and small business customers is only beginning to take hold in Illinois. Competitive entry is at nascent and precarious levels. Z-Tel, a company focused on residential and small business services, has chosen to make Illinois one of its key target markets in the coming year because of the competitive opportunities offered by the Commission, the Merger Conditions, and the recent telecommunications law re-write. Z-Tel's initial market success is, however, threatened if SBC/Ameritech is allowed to stack the deck. Eliminating Merger Condition 26 in favor of a potentially inadequate and certainly discriminatory rebate scheme could tip the competitive advantage to SBC/Ameritech at this crucial juncture.

In the long run, consumers would benefit far more from increased competitive choice and innovation than a one-time dinner-and-a-movie rebate.

Accordingly, the Z-Tel respectfully requests that the Commission deny the Joint Motion to Reopen the Record, and Merger Condition 26 should remain in place.

Respectfully submitted,

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